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Privity Revisited: Tort Recovery by a Commercial Buyer for a Defective Product's Self-Inflicted Damage

The relationship between the warranty provisions of the Uniform Commercial Code¹ and strict tort liability for physical harm² caused by a defective product has been the source of considerable controversy.³ Virtually all states allow the buyer of a defective product a cause of action based on both theories.⁴ The theoretical justifications for the tort remedy, however, are different from those supporting the essentially contractual⁵ warranty remedy.⁶ While the remedies overlap significantly, they are not coextensive.⁷ Establishing the boundary between them has proved very difficult.⁸

One important aspect of this boundary-drawing process is deter-

1. U.C.C. §§ 2-313 to 2-318 (1978); *see also* U.C.C. § 2-719(3) (limitation of warranty to exclude personal injuries is prima facie unconscionable in the case of consumer goods); U.C.C. § 2-302 (unconscionability generally).

2. Physical harm includes personal injuries and property damage. *See* RESTATEMENT (SECOND) OF TORTS § 7(3) (1965) (defining physical harm); *see also* Seely v. White Motor Co., 63 Cal. 2d 9, 19, 403 P.2d 145, 152, 45 Cal. Rptr. 17, 24 (1965) (strict tort liability includes physical injury to property as well as personal injury).

3. *See, e.g.,* Franklin, *When Worlds Collide: Liability Theories and Disclaimers in Defective-Product Cases*, 18 STAN. L. REV. 974 (1966); Rapson, *Products Liability Under Parallel Doctrines: Contrasts Between the Uniform Commercial Code and Strict Liability in Tort*, 19 RUTGERS L. REV. 692 (1965); Titus, *Restatement (Second) of Torts Section 402A and the Uniform Commercial Code*, 22 STAN. L. REV. 713 (1970); Wade, *Tort Liability for Products Causing Physical Injury and Article 2 of the U.C.C.*, 48 MO. L. REV. 1 (1983); Note, *Economic Loss in Products Liability Jurisprudence*, 66 COLUM. L. REV. 917 (1966) [hereinafter cited as Note, *Economic Loss*]; Note, *Products Liability in Commercial Transactions*, 60 MINN. L. REV. 1061 (1976); Note, *Torts — Products Liability — Should Contract or Tort Provide the Cause of Action When a Plaintiff Seeks Recovery Only for Damage to the Product Itself*, 10 N. KY. L. REV. 489 (1983) [hereinafter cited as Note, *Contract or Tort*].

4. Louisiana is the only state that has not adopted Article 2 of the U.C.C. The Delaware Supreme Court has held that the state legislature's adoption of the U.C.C. preempted judicial adoption of strict tort liability. *Cline v. Prowler Indus.*, 418 A.2d 968, 975 (Del. 1980). The Massachusetts Supreme Judicial Court has reached a similar result. *See Back v. Wickes Corp.*, 375 Mass. 633, 640, 378 N.E.2d 964, 969 (1978); *Swartz v. General Motors Corp.*, 375 Mass. 628, 629, 378 N.E.2d 61, 62 (1978) (breach of warranty under Massachusetts U.C.C. provides as comprehensive a remedy as strict tort liability). *See generally* 1 R. HURSH & H. BAILEY, *AMERICAN LAW OF PRODUCTS LIABILITY* § 4:41 (2d ed. 1974 & Supp. 1985).

5. *See* Part II. A *infra*.

6. Contract law rests on obligations imposed by the parties to the contract. It seeks to put the plaintiff in the position he or she would have been in had the defendant fully performed. *See* U.C.C. § 1-106 (1978). Tort law rests on obligations imposed by law. It seeks to restore the plaintiff to the position he or she was in before being injured by the defendant's wrongful conduct. *See* Wade, *supra* note 3, at 24; *see also* *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1169 (3d Cir. 1981) (discussed in text at notes 18-21 *infra*).

7. *See* J. WHITE & R. SUMMERS, *HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE* 325 (2d ed. 1980).

8. *See* Wade, *supra* note 3, at 26 n.87; *see also* W. Prosser, *The Borderland of Tort and Contract*, in *SELECTED TOPICS ON THE LAW OF TORTS* 380 (1953); *cf.* G. GILMORE, *THE DEATH OF CONTRACT* (1974).

mining which items of damages are recoverable under which theory.⁹ In particular, economic losses — e.g., damages for inadequate value, costs of repair, and replacement of defective goods, or for consequent loss of profits¹⁰ — generally cannot be recovered in a tort action.¹¹ These losses represent the buyer's contractual expectation interest, and the buyer's remedy, if any, must be based on the product's warranty.¹²

Tort and contract principles come into conflict when the product itself is damaged or destroyed as the result of its own defect.¹³ The product is the buyer's property, and damages for physical harm to property are recoverable in tort.¹⁴ However, the value of the product itself is the central element in the parties' bargain. As part of that bargain, the parties may have allocated the risks of a defect. The premises of contract law are abandoned if a buyer may evade contractual language excluding or limiting warranty liability simply by suing the seller in tort.¹⁵

This Note argues that if a seller and a commercial buyer are in privity, damage to a product resulting from its own defect should not be recoverable by a commercial buyer in a tort action. Part I shows

9. See, e.g., *Rudd Constr. Equip. Co. v. Clark Equip. Co.*, 735 F.2d 974, 983 (6th Cir. 1984); *Mid Continent Aircraft v. Curry County Spraying Serv.*, 572 S.W.2d 308 (Tex. 1978).

10. See J. WHITE & R. SUMMERS, *supra* note 7, at 405; Note, *Economic Loss*, *supra* note 3, at 917. Various definitions of economic loss have been applied by courts and commentators. See generally Note, *Products Liability: Expanding the Property Damage Exception in Pure Economic Loss Cases*, 54 CHI.-KENT L. REV. 963, 963 n.2 (1978).

11. The leading case espousing this view is *Seely v. White Motor Co.*, 63 Cal. 2d 9, 403 P.2d 145, 45 Cal. Rptr. 17 (1965). *Contra* *Santor v. A & M Karagheusian, Inc.*, 44 N.J. 52, 207 A.2d 305 (1965). See generally Comment, *Strict Liability: Recovery of "Economic" Loss*, 13 IDAHO L. REV. 29, 40 (1976); Note, *Manufacturer's Strict Tort Liability to Consumers for Economic Loss*, 41 ST. JOHN'S L. REV. 401, 405 (1967).

12. See, e.g., *Jones & Laughlin Steel Corp. v. Johns-Manville Sales Corp.*, 626 F.2d 280 (3d Cir. 1980); *Fredonia Broadcasting Corp. v. RCA Corp.*, 481 F.2d 781 (5th Cir. 1973); *Southwest Forest Indus. v. Westinghouse Elec. Corp.*, 422 F.2d 1013 (9th Cir.), *cert. denied*, 400 U.S. 902 (1970); *Plainwell Paper Co. v. Pram, Inc.*, 430 F. Supp. 1386 (W.D. Pa. 1977); *Arizona v. Cook Paint & Varnish Co.*, 391 F. Supp. 962 (D. Ariz. 1975), *aff'd*, 541 F.2d 226 (9th Cir. 1976), *cert. denied*, 430 U.S. 915 (1977); *Seely v. White Motor Co.*, 63 Cal. 2d 9, 403 P.2d 145, 45 Cal. Rptr. 17 (1965); *Clark v. International Harvester Co.*, 99 Idaho 326, 581 P.2d 784 (1978); *National Crane Corp. v. Ohio Steel Tube Co.*, 213 Neb. 782, 332 N.W.2d 39 (1983); *Mid Continent Aircraft v. Curry County Spraying Serv.*, 572 S.W.2d 308 (Tex. 1978).

13. See Wade, *supra* note 3, at 26 n.87.

14. See note 2 *supra*; see also *Industrial Uniform Rental Co. v. International Harvester Co.*, 317 Pa. Super. 65, 80, 463 A.2d 1085, 1093 (1983) (Hester, J., dissenting); *Air Prods. & Chems. v. Fairbanks Morse, Inc.*, 58 Wis. 2d 193, 217-19, 206 N.W.2d 414, 426-28 (1973).

15. *Rudd Constr. Equip. Co. v. Clark Equip. Co.*, 735 F.2d 974, 984 (6th Cir. 1984) ("[W]e do not believe that a sophisticated, commercial buyer . . . can evade contractual language excluding liability for consequential or special damages simply by suing the seller in tort."); see also *Daitom, Inc. v. Pennwalt Corp.*, 741 F.2d 1569, 1582 (10th Cir. 1984) ("The extension of products liability to these types of losses would make the manufacturer the guarantor that its products would continue to perform satisfactory [sic] throughout their productive lives. This is plainly against the purpose of either current manufacturer's products liability or contract law."); *Twin Disc, Inc. v. Big Bud Tractor, Inc.*, 582 F. Supp. 208, 214 (E.D. Wis. 1984) ("To allow tort remedies to overlay this commercial framework . . . would undermine certainty and predictability in business relationships . . .").

how the conflict arises and examines the judicial boundaries that are normally drawn between tort and warranty liability. Part II contrasts the rationales for the warranty and tort remedies, with particular emphasis on the Uniform Commercial Code and Section 402A of the *Restatement (Second) of Torts*. Part III argues that if a seller and a commercial buyer are in privity and the only damage is to the defective product itself, the rationales supporting strict tort liability are inapplicable. The Note concludes that commercial buyers seeking to recover the value of a product that has been damaged as a result of its own defect should be limited to the remedies provided by the Uniform Commercial Code in a suit against their immediate sellers.

I. PHYSICAL DAMAGE AND THE ECONOMIC-LOSS RULE

The buyer of a defective product can always seek a remedy under the Uniform Commercial Code. If some provision of the Code bars or limits recovery,¹⁶ the buyer may seek to circumvent the troublesome Code provision by suing under the strict tort liability theory. Ordinarily, if there is physical damage to persons or property, the policies underlying strict tort liability are sufficiently strong to permit recourse to tort law as an alternate theory of recovery.¹⁷ However, if the only damage caused by the defective product is to the product itself — that is, if the physical damage is self-inflicted — the policies supporting an action based on strict tort liability are far less compelling.

The facts in *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*¹⁸ illustrate the conflict between the Uniform Commercial Code warranty provisions and strict tort liability. Pennsylvania Glass Sand (PGS) bought a front-end loader from Caterpillar in 1971. The express warranty accompanying the loader limited the purchaser's remedy to replacement of defective parts and specifically excluded recovery for economic loss.¹⁹ For approximately four years, PGS used the loader daily at its quarry in Mapleton, Pennsylvania. In September 1975 a fire broke out near the loader's hydraulic lines. The operator escaped injury, but neglected to turn the machine off. As a result, hydraulic fluid continued to fuel the fire, causing severe damage to the loader.

In June 1979 PGS filed suit seeking as damages the amount spent on repairing the loader and securing a temporary replacement. Liability for these damages was specifically excluded by Caterpillar's war-

16. See notes 55-59 *infra* and accompanying text.

17. *E.g.*, *Sanco, Inc. v. Ford Motor Co.*, 579 F. Supp. 893, 897 (S.D. Ind. 1984) (noting in dicta: "Imposing tort liability on a manufacturer . . . is justified when a product causes personal injury or even when it causes damage to itself or other property under circumstances in which the absence of personal injury is merely fortuitous . . ."), *aff'd.*, 771 F.2d 1081 (7th Cir. 1985).

18. 652 F.2d 1165 (3d Cir. 1981) (applying Pennsylvania law).

19. 652 F.2d at 1167.

ranty. Moreover, as the court noted, by the time suit was filed, a warranty claim was probably barred by the Code's statute of limitations.²⁰ Nevertheless, by advancing theories of negligence and strict tort liability, PGS was able to proceed to trial.²¹

Because of the existence of both tort and contract remedies for personal injuries and property damage, courts face a "seamless web running from express warranty through the implied warranty of merchantability to strict tort liability."²² The tort theory offers an important advantage to buyers because, in a tort action, the various Code defenses²³ are not available to the seller. Since the issue of liability and the amount of recovery may depend on which theory is successful, courts entertaining both theories in a single suit have been forced to define the contours of the developing tort remedy.²⁴

It is generally accepted that economic losses,²⁵ at least when unaccompanied by any physical damage,²⁶ are not recoverable in an action based on strict tort liability.²⁷ The rationale for this rule is that the buyer's economic interests are adequately protected by the Code,²⁸ and subjecting a seller to strict liability for exclusively economic losses would displace the legislatively enacted Code framework.²⁹ Moreover, imposing tort liability would result in "the consuming public [paying] more for their products so that a manufacturer can insure against the possibility that some of his products will not meet the business needs of some of his customers."³⁰

In many situations, the economic-loss rule can be applied without

20. 652 F.2d at 1167 n.2.

21. 652 F.2d at 1176.

22. J. WHITE & R. SUMMERS, *supra* note 7, at 325.

23. See notes 55-59 *infra* and accompanying text.

24. See, e.g., *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1169-73 (3d Cir. 1981) (tracing the development of strict tort liability and the economic-loss doctrine).

25. For the purposes of this analysis, economic losses are defined as damages for inadequate value, costs of repair and replacement of the defective product, or consequent loss of profits. See note 10 *supra* and accompanying text.

26. See note 2 *supra*.

27. See, e.g., *Seely v. White Motor Co.*, 63 Cal. 2d 9, 403 P.2d 145, 45 Cal. Rptr. 17 (1965). But see, e.g., *Santor v. A & M Karagheusian, Inc.*, 44 N.J. 52, 207 A.2d 305 (1965).

28. See, e.g., *Clark v. International Harvester Co.*, 99 Idaho 326, 336, 581 P.2d 784, 794 (1978).

29. E.g., *Moorman Mfg. Co. v. National Tank Co.*, 91 Ill. 2d 69, 91, 435 N.E.2d 443, 453 (1982) (commercial buyer limited to U.C.C. remedies for cracks developing in a defective silo).

30. *Seely v. White Motor Co.*, 63 Cal. 2d 9, 19, 403 P.2d 145, 151, 45 Cal. Rptr. 17, 23 (1965).

The mechanism by which a seller can pass these insurance costs on to a buyer is considerably more complicated than first appears. Apparently the benchmark cost of insuring against products liability now stands at about one percent of sales, although there are, of course, major variations among industries. See Schwartz, *New Products, Old Products, Evolving Law, Retroactive Law*, 58 N.Y.U. L. REV. 796, 812 & n.114 (1983); see also INTERAGENCY TASK FORCE ON PRODUCT LIABILITY, U.S. DEPT. OF COMMERCE, FINAL REPORT (1978). The one percent figure does not reflect the cumulative effect of the cost of products liability insurance as the product

difficulty. It is reasonably clear that the "operation of a defective radiator causes property damage when it results in a fire which destroys the plaintiff's store and economic harm when it results in conditions so uncomfortable that it causes the loss of customer patronage."³¹ Damages to the store could be recovered in a tort suit, while damages for lost profits would be recoverable, if at all, in contract.³² But if a product is damaged as a result of its own defects — if, for example, the radiator becomes clogged because of a defective valve — the property damage is coextensive with the economic loss. In such cases, the economic-loss rule's "type of harm" criterion provides no guidance on whether a tort remedy should be available.

Courts have taken four different approaches to determining whether a tort recovery is available for a product's self-inflicted damages. Two of those approaches simply read the economic-loss rule as if it *did* provide guidance. The fact that economic loss is coincident with physical damage does not make it any the less economic loss, and one approach is to deny recovery for a defective product's self-inflicted damage for that reason.³³ A second approach reaches the opposite conclusion by essentially the same logic: the fact that a defective product's self-inflicted damage is coincident with economic loss does not make it any the less physical damage, or any the less recoverable in a tort action.³⁴ Clearly, neither of these approaches provides a princi-

passes through the chain of distribution, nor does it reflect indirect costs borne by the insured, such as claims handling and deductibles. *Id.* at VI-23 to VI-24.

Depending on a firm's profit margin, it may or may not be able to absorb the cost of insuring against products liability, *see id.* at VI-12 to VI-13, and, depending on the elasticity of demand for a firm's products, it may or may not be able to pass these costs on to its buyers. *But cf.* H. VARIAN, MICROECONOMIC ANALYSIS 63-64 (1978) (In a competitive market, whether a tax is levied on a producer or a consumer makes no difference in the short run; in the long run, the price to the consumer will have to rise by exactly the amount of the tax.).

31. Note, *Economic Loss*, *supra* note 3, at 918.

32. *But see, e.g.*, *Union Oil Co. v. Oppen*, 501 F.2d 558 (9th Cir. 1974) (commercial fishermen allowed to recover for economic losses resulting from an oil spill caused by oil company's negligence).

33. *E.g.*, *St. Paul Fire & Marine Ins. Co. v. Steeple Jac Inc.*, 352 N.W.2d 107 (Minn. Ct. App. 1984) (damage to a window washing unit resulting from a fall caused by the unit's own defective gear box not recoverable under negligence or strict tort liability theories, even when the defect creates an unreasonable danger to persons or other property); *Mid Continent Aircraft v. Curry County Spraying Serv.*, 572 S.W.2d 308 (Tex. 1978) (no tort recovery for buyer of a rebuilt airplane, damaged in a forced landing after its engine failed, when there were no personal injuries or damages to property other than the airplane itself).

34. The leading case espousing this approach is *Santor v. A & M Karagheusian, Inc.*, 44 N.J. 52, 207 A.2d 305 (1965). Cases in other jurisdictions adopting the *Santor* approach include *Mead Corp. v. Allendale Mut. Ins. Co.*, 465 F. Supp. 355, 363-66 (N.D. Ohio 1979) (allowing commercial buyer to recover under strict liability in tort for direct and indirect economic losses due to defective steam turbine); *Cova v. Harley Davidson Motor Co.*, 26 Mich. App. 602, 608-09, 182 N.W.2d 800, 804 (1970) (allowing owners of golf course to recover against manufacturer in strict liability for economic losses resulting from defects in golf carts); *Iacono v. Anderson Concrete Corp.*, 42 Ohio St. 2d 88, 91-93, 326 N.E.2d 267, 269-71 (1975) (allowing homeowner to maintain an action in tort for damage to concrete driveway due to defective materials and workmanship); *City of La Crosse v. Schubert*, 72 Wis. 2d 38, 44-45, 240 N.W.2d 124, 127 (1976)

pled basis for allowing or disallowing recovery for self-inflicted damages.

Not surprisingly, a majority of courts have turned to a third approach, based upon the landmark decision of *Seely v. White Motor Co.*³⁵ The *Seely* court reasoned that a requirement for the imposition of strict tort liability is the existence of an unreasonably dangerous defect, so that only contractual remedies should be available for ordinary qualitative defects.³⁶ Thus, when the damage to the defective product results from deterioration or some other gradual, nonaccidental cause, it is characterized as economic loss, and any remedies must be found in the Code.³⁷ When a product defect causes the product to sustain physical harm in a violent or sudden manner, the damage is characterized as property damage, and the manufacturer also will be liable in tort.³⁸ The rationale is that when a product defect creates a risk of personal injury, liability should not depend upon the fortuity of whether or not personal injuries actually occurred.³⁹

(permitting tort recovery from manufacturer of defective roofing materials for loss of value of roof and, in dicta, also for consequential economic damages). In *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 98 N.J. 555, 489 A.2d 660 (1985), the New Jersey Supreme Court held that the *Santor* holding did not extend to commercial buyers. The plaintiff, a distributor in the business of selling and leasing trucks, was thus limited to its Code remedies.

35. 63 Cal. 2d 9, 403 P.2d 145, 45 Cal. Rptr. 17 (1965).

36. [The manufacturer] can appropriately be held liable for physical injuries caused by defects by requiring his goods to match a standard of safety defined in terms of conditions that create unreasonable risks of harm. . . . [The consumer] can . . . be fairly charged with the risk that the product will not match his economic expectations unless the manufacturer agrees that it will.

63 Cal. 2d at 18, 403 P.2d at 151, 45 Cal. Rptr. at 23. In *Seely*, the plaintiff bought a truck from the defendant, White Motor Company. Upon taking possession of the truck, the buyer found that it bounced violently, a condition known as "galloping." The seller's representatives made many unsuccessful efforts to correct the problem. Later, faulty brakes caused the buyer's truck to overturn, resulting in damage to the truck but no personal injuries. The buyer sued the seller for (1) accident-related damages for the repair of the truck, and (2) damages, unrelated to the accident, for the money paid on the purchase price and for the profits lost in his business because he was unable to make normal use of the truck. The California Supreme Court affirmed a judgment awarding the plaintiff the second category of damages based on breach of warranty, but denying the plaintiff's strict tort liability claim for the accident-related damages.

37. See *Morrow v. New Moon Homes, Inc.*, 548 P.2d 279 (Alaska 1977) (disallowing action based on strict tort liability against a mobile home manufacturer to recover damages for defects such as a faulty furnace, doors that would not close, cracked windows, a malfunctioning electrical system, a leaky bathtub, and a leaky roof, because the defects resulted only in economic losses).

38. See *Cloud v. Kit Mfg. Co.*, 563 P.2d 248 (Alaska 1977) (allowing action based on strict tort liability against a mobile home manufacturer for damages to the mobile home resulting from a fire caused by the product's own defect).

39. See *Largoza v. General Elec. Co.*, 538 F. Supp. 1164, 1169 (E.D. Pa. 1982) ("It would surely be anomalous if manufacturers were allowed to evade their responsibility to market safe products merely because of the fortuitous circumstances that loss of life did not result on a particular occasion."); *Seely v. White Motor Co.*, 63 Cal. 2d 9, 22 n.2, 403 P.2d 145, 154 n.2, 45 Cal. Rptr. 17, 26 n.2 (1965) (Peters, J., concurring) ("I cannot rationally hold that the plaintiff whose vehicle is destroyed in an accident caused by a defective part may recover his property damage under a given theory while another plaintiff who is astute or lucky enough to discover the defect and thereby avoid such an accident cannot recover for other damages proximately

The *Seely* approach provides a principled basis for delineating the limits of the economic-loss rule by refining the "type of harm" concept. In practice, however, this means that courts must make their own assessments of the sort of risks that may have been posed by particular defects. Moreover, the *Seely* approach allows contractual arrangements to be upset depending on how suddenly an economic loss is incurred.⁴⁰ A fourth approach obviates both speculation and fortuity by returning to a fundamental distinction: Contract law, unlike tort law, is predicated on a bargain between two parties.⁴¹ If the risk which in fact materialized was the subject of contractual risk allocation,⁴² using tort law to shift losses subverts the rationale for the economic-loss rule. Under this approach, the key factor is whether the buyer and seller were in privity,⁴³ and thus in a position to allocate the risks of self-inflicted damage to defective products.⁴⁴ If they were, tort

caused by an identical defective part. The strict liability should apply to both plaintiffs or to neither. They cannot be validly distinguished."); Comment, *The Vexing Problem of the Purely Economic Loss in Products Liability: An Injury in Search of a Remedy*, 4 SETON HALL L. REV. 145, 154 (1972); cf. *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1173 (3d Cir. 1981) ("[T]he line between tort and contract must be drawn by analyzing inter-related factors such as the nature of the defect, the type of risk, and the manner in which the injury arose.").

40. See *Consumers Power Co. v. Curtiss-Wright Corp.*, 780 F.2d 1093, 1102 (3d Cir. 1986) (Weis, J., dissenting):

[E]conomic loss, including damage to the product itself, is a matter for negotiation and allocation of risk between the parties. The fortuity that personal injury or outside property damage might occur in addition to injury to the defective product does not require a different rule with respect to economic loss.

41. See *Seely v. White Motor Co.*, 63 Cal. 2d 9, 26, 403 P.2d 145, 156, 45 Cal. Rptr. 17, 28 (1965) (Peters, J., concurring) ("How can the nature of the damages which occur later, long after the transaction has been completed, control the characterization of the transaction? Any line which determines whether damages should be covered by warranty law or the strict liability doctrine should be drawn at the time the sale is made.") (emphasis in original).

42. In *Consumers Power Co. v. Curtiss-Wright Corp.*, 780 F.2d 1093 (3d Cir. 1986), the court upheld a tort recovery for the value of an engine that exploded due to a faulty replacement part, in part because "no limitation of liability had been agreed to by the parties. They did not shift the economic risk of an accident by agreement from what the parties could expect under ordinary tort principles." 780 F.2d at 1099. That the parties are entitled to limit liability by mutual agreement, however, demonstrates that their relationship is essentially contractual. It cannot be that the question of whether the U.C.C. applies, to the exclusion of strict tort liability, depends upon whether the parties have agreed to an express limitation of liability. Cf. note 44 *infra*.

43. Originally, lack of privity was grounds for dismissing a tort claim. See note 66 *infra*. This new approach thus stands the old privity limitation on its head, by requiring dismissal of tort claims if the parties are in privity.

44. Whether genuine bargaining can occur also depends, of course, on the relative strength of the parties. Some courts have held strict tort liability inapplicable between parties who "(1) deal in a commercial setting; (2) from positions of relatively equal economic strength; (3) bargain the specifications of the product; and (4) negotiate concerning the risk of loss from defects in it." *Kaiser Steel Corp. v. Westinghouse Elec. Corp.*, 55 Cal. App. 3d 737, 748, 127 Cal. Rptr. 838, 845 (1976); see also *Purvis v. Consolidated Energy Prods. Co.*, 674 F.2d 217 (4th Cir. 1982); *Scandinavian Airlines Sys. v. United Aircraft Corp.*, 601 F.2d 425 (9th Cir. 1979). This Note argues that, although the consumer/commercial buyer distinction is problematic, see note 144 *infra*, the privity approach is properly limited to disputes involving commercial buyers.

Demanding evidence of actual negotiation about loss due to product defects — rather than

remedies are unavailable, regardless of the way the damage occurred.⁴⁵

The economic-loss rule does not itself provide an answer to the problem of a product's self-inflicted damage. The inconsistent results it has yielded in federal court diversity cases, where a buyer's recovery may depend on complicated choice-of-law questions and tenuous predictions of state law, highlight the need for a workable and uniform rule.⁴⁶ In cases involving commercial buyers, such a rule can be developed from an analysis of the different policies underlying strict tort liability and the Uniform Commercial Code.

II. WARRANTY AND STRICT LIABILITY IN TORT: THE DEVELOPMENT OF PARALLEL THEORIES OF RECOVERY

The justifications for strict liability in tort are distinct from the policies underlying the Uniform Commercial Code. The Code relies on market processes to reach a socially desirable outcome. It defers to the intentions of the parties because it presumes that they have adequate information and sufficient bargaining power to reach an agreement that advances the interests of the buyer, the seller, and society at large. In contrast, strict liability in tort contemplates a failure of market processes. Losses are allocated by rule of law because transaction costs, information costs, or external costs prevent the parties from reaching a socially desirable outcome.

simply the ability to bargain — is question-begging, for the issue is whether a *nonconsensual* tort remedy should be imposed upon the parties. See notes 88-93 *infra* and accompanying text. If both parties have effective bargaining power, and do not use it to negotiate about risk of loss, they have chosen to avail themselves of the law that will apply in default of a contractual provision. What that law is should not vary depending on whether negotiation occurred.

45. *E.g.*, *Twin Disc, Inc. v. Big Bud Tractors, Inc.*, 582 F. Supp. 208 (E.D. Wis. 1984) (denying negligence and strict tort liability claims against manufacturer of allegedly defective transmissions where plaintiff tractor manufacturer was not a consumer or ultimate user, and the parties were in privity); *General Pub. Utils. Corp. v. Babcock & Wilcox Co.*, 547 F. Supp. 842 (S.D.N.Y. 1982) (plaintiffs, owners and operators of Three Mile Island nuclear generating facility denied strict tort liability claim against manufacturer of allegedly defective nuclear steam supply system where, *inter alia*, the parties were in contractual privity and were in a position to allocate risk).

46. See *Rudd Constr. Equip. Co. v. Clark Equip. Co.*, 735 F.2d 974, 978 (6th Cir. 1984):

This appeal demonstrates the problems faced in diversity cases when federal courts must predict state law without the security of appellate review by the state's highest court. The problem is particularly acute here, given the dearth of authority in Kentucky law on some of the issues, and the considerable variation in the treatment of like issues by the courts of different states.

See also *C & S Fuel, Inc. v. Clark Equip. Co.*, 524 F. Supp. 949, 952 (E.D. Ky. 1981) (emphasis in original):

[T]he Court is not unmindful of the . . . [seller's] forceful policy arguments in refusing to recognize a cause of action in tort. However, at this juncture, the superseding policy of uniform application of the law compels only one result. Were this court to grant the defendant's motion, it would result in declaring *the same defendant for the same conduct* not liable in half of this Commonwealth, and liable in the other half.

Courts,⁴⁷ commentators,⁴⁸ and draftsmen⁴⁹ have emphasized that the tort and Code remedies, like the theories underlying them, are distinct. Both schemes advance social interests only to the extent that their underlying assumptions are valid. Which damages are available thus depends upon whether the assumptions underlying the Code or those underlying strict tort liability are more likely to hold true when a product is damaged as a result of its own defect.

A. Breach of Warranty Under the Uniform Commercial Code

A buyer's action for breach of warranty is governed generally by the Uniform Commercial Code. Three of the Code's four warranty provisions are relevant to cases involving defective products.⁵⁰ The Code controls express warranties, which are created by the parties as part of their bargain.⁵¹ It also creates an implied warranty of merchantability⁵² and, under certain circumstances, an implied warranty of fitness for a particular purpose.⁵³

The Code's damage provisions are broad enough to provide relief for all injuries to person or property caused by a defective product, including damage to the product itself.⁵⁴ Nevertheless, a buyer attempting to recover under these Code provisions still faces significant obstacles. First, a seller may limit the remedies available for breach of

47. See, e.g., *C & S Fuel, Inc. v. Clark Equip. Co.*, 524 F. Supp. 949, 952 (E.D. Ky. 1981) (noting that the "elements of a cause of action in tort for property damage loss differ from the elements in contract"); *Seely v. White Motor Co.*, 63 Cal. 2d 9, 15, 403 P.2d 145, 149, 45 Cal. Rptr. 17, 21 (1965) ("The history of the doctrine of strict liability in tort indicates that it was designed, not to undermine the warranty provisions of the . . . Uniform Commercial Code but, rather, to govern the distinct problem of physical injuries.").

48. See, e.g., *Wade*, *supra* note 3, at 24-26.

49. See U.C.C. § 2-318 comment 3 (1978); RESTATEMENT (SECOND) OF TORTS § 402A comment m (1964).

50. See generally *J. WHITE & R. SUMMERS*, *supra* note 7, at 325-74. The provision relating to warranty of title, U.C.C. § 2-312 (1978), is not germane in products liability cases.

51. U.C.C. § 2-313 (1978).

52. U.C.C. § 2-314 (1978). Section 2-314(3) also provides that "other implied warranties may arise from course of dealing or usage of trade."

53. U.C.C. § 2-315 (1978) provides:

Where the seller at the time of contracting has reason to know any particular purpose for which the goods are required and that the buyer is relying on the seller's skill or judgment to select or furnish suitable goods, there is unless excluded or modified under [2-316] an implied warranty that the goods shall be fit for such purpose.

54. See *Wade*, *supra* note 3, at 2. Although U.C.C. § 2-714(2) states that the measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods as accepted and the value they would have had if they had been as warranted, U.C.C. § 2-714 comment 3 (1978) states that § 2-714(2) "describes the usual, standard and reasonable method of ascertaining damages in the case of breach of warranty but it is not intended as an exclusive measure." Section 2-714(3) provides that "[i]n a proper case . . . consequential damages may also be recovered." Section 2-715(2) states that "[c]onsequential damages resulting from the seller's breach include . . . injury to person or property proximately resulting from any breach of warranty." Thus, damage to the defective product resulting from its own defect would be an element of consequential damages. See *J. WHITE & R. SUMMERS*, *supra* note 7, at 386-87 & n.54.

warranty.⁵⁵ Second, implied warranties may be disclaimed entirely.⁵⁶ Third, the buyer must "within a reasonable time after he discovers or should have discovered" a breach of warranty, give notice of the breach "or be barred from any remedy."⁵⁷ Finally, a breach of warranty normally occurs when tender of delivery is made,⁵⁸ and an action for the breach must be commenced within four years thereafter.⁵⁹

The Uniform Commercial Code, like contract law generally, regulates economic transactions such as buying, selling, leasing, and borrowing. The underlying economic principle is that rational decisionmakers will make exchanges that maximize utility.⁶⁰ In the process, resources are allocated to their most valuable uses, thus maximizing the wealth of society as well.⁶¹ Consistent with the goal of facilitating such voluntary exchanges, the underlying policies of the Uniform Commercial Code are to simplify, clarify, and modernize the law of commercial transactions; permit the continued expansion of commercial practices; and encourage uniform commercial laws.⁶²

55. U.C.C. § 2-316(4) (1978); *see also* U.C.C. §§ 2-718 to 2-719 (1978); U.C.C. § 2-719 comment 3 (1978) ("clauses limiting or excluding consequential damages . . . are merely an allocation of unknown or undeterminable risks").

56. U.C.C. § 2-316(2) & (3) (1978). A common example of such a disclaimer is the case of a product sold "as is." U.C.C. § 2-316(3)(a) (1978). *See* *Mid Continent Aircraft v. Curry County Spraying Serv.*, 572 S.W.2d 308, 313 (Tex. 1978).

57. U.C.C. § 2-607(3)(a) (1978). *See* *Greenman v. Yuba Power Prods.*, 59 Cal. 2d 57, 377 P.2d 897, 27 Cal. Rptr. 697 (1963) (discussing notice requirements under the Uniform Sales Act, predecessor of the U.C.C.).

58. U.C.C. § 2-725(2) (1978). An exception is made "where a warranty explicitly extends to future performance." *See, e.g.,* *Moorman Mfg. Co. v. National Tank Co.*, 91 Ill. 2d 69, 92-95, 435 N.E.2d 443, 453-54 (1982).

59. U.C.C. § 2-725(1) (1978). The limitation period for tort claims starts to run only when the accident occurs, and thus may extend much longer. *See, e.g.,* *Cinnaminson Twp. Bd. of Educ. v. U.S. Gypsum Co.*, 552 F. Supp. 855, 858-63 (D.N.J. 1982); *see also* notes 121 & 149 *infra*.

60. *See* A. KRONMAN & R. POSNER, *THE ECONOMICS OF CONTRACT LAW* 1-2 (1979).

61. *See id.* at 2 (footnote omitted):

If A owns a good that is worth only \$100 to him but \$150 to B, both will be made better off by an exchange of A's good for B's money at any price between \$100 and \$150; and if they realize this, they will make the exchange. By making both of them better off, the exchange will also increase the wealth of society (of which they are members), assuming the exchange does not reduce the welfare of nonparties more than it increases A's and B's welfare. Before the exchange — which, let us say, takes place at a price of \$125 — A had a good worth \$100 to him and B had \$125 in cash, a total of \$225. After the exchange, A has \$125 in cash and B has a good worth \$150 to him, a total of \$275. The exchange has increased the wealth of society by \$50 (ignoring, as we have done, any possible third-party effects).

Stated another way, voluntary exchanges enhance economic efficiency. The classic criterion for economic efficiency is Pareto superiority, a term that describes an exchange that makes at least some people better off without making anyone worse off. Kronman and Posner employ the more modern and less stringent Kaldor-Hicks criterion, under which an exchange is efficient if it is *potentially* Pareto superior; *i.e.*, the people who are better off *could* compensate those who are worse off out of their gains. *See* H. VARIAN, *MICROECONOMIC ANALYSIS* 216 (1978). *But see* Note, *Efficiency and a Rule of "Free Contract": A Critique of Two Models of Law and Economics*, 97 HARV. L. REV. 978 (1984).

62. U.C.C. § 1-102(2)(a)-(c) (1978).

Freedom of contract is a principle of the Code,⁶³ and its remedies are designed to put the aggrieved party in as good a position as if the other party had fully performed the agreement.⁶⁴

B. *Strict Tort Liability: Beyond the Warranty Fiction*

The liability of a remote manufacturer in connection with the sale of a defective product began to develop early in the twentieth century.⁶⁵ Under the previous rule, if the aggrieved buyer was not in privity with the manufacturer, no recovery could be had, not even for negligence.⁶⁶ Once the privity limitation was discarded for negligence, however, courts began to carry the manufacturer's responsibility further.⁶⁷ Liability without negligence and without privity was first established in cases involving unsafe food and drink.⁶⁸ Later, this liability was extended to animal food,⁶⁹ cosmetics,⁷⁰ and other products,⁷¹ eventually resulting in the formulation of the current doctrine of strict liability in tort.⁷²

Courts relied on a variety of legal theories to support the extension

63. U.C.C. § 1-102 comment 2 (1978).

64. U.C.C. § 1-106(1) (1978).

65. See *MacPherson v. Buick Motor Co.*, 217 N.Y. 382, 111 N.E. 1050 (1916) (Cardozo, J.).

66. The privity requirement can be traced to Lord Abinger's broad language in *Winterbottom v. Wright*, 152 Eng. Rep. 402, 10 M. & W. 109 (1842), which was taken to mean that the original seller of goods was not liable for damages to anyone except his immediate buyer. Today the rule seems to be crumbling away, with current vitality primarily in the economic loss cases. See J. WHITE & R. SUMMERS, *supra* note 7, at 399-411; Prosser, *The Fall of the Citadel (Strict Liability to the Consumer)*, 50 MINN. L. REV. 791 (1966); Prosser, *The Assault Upon the Citadel (Strict Liability to the Consumer)*, 69 YALE L.J. 1099 (1960) [hereinafter cited as Prosser, *The Assault*].

67. See generally W. PROSSER & W. KEETON, *THE LAW OF TORTS* § 97 (5th ed. 1984).

68. *Mazetti v. Armour & Co.*, 75 Wash. 622, 135 P. 633 (1913); see also Prosser, *The Assault*, *supra* note 66, at 1105-06 nn.39-40. Influential in this development was Upton Sinclair's *The Jungle*, which provided a fictional account of abuses in the meat-packing industry.

69. *E.g.*, *McAfee v. Cargill, Inc.*, 121 F. Supp. 5 (S.D. Cal. 1954).

70. *E.g.*, *Graham v. Bottenfield's, Inc.*, 176 Kan. 68, 269 P.2d 413 (1954).

71. *E.g.*, *Spence v. Three Rivers Builders & Masonry Supply*, 353 Mich. 120, 90 N.W.2d 873 (1958) (cinder block building material).

72. While strict liability in tort varies from state to state, the most authoritative statement of the doctrine is found in the RESTATEMENT (SECOND) OF TORTS § 402A, which provides:

(1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if

(a) the seller is engaged in the business of selling such a product, and

(b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.

(2) The rule stated in Subsection (1) applies although

(a) the seller has exercised all possible care in the preparation and sale of his product, and

(b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

See also J. WHITE & R. SUMMERS, *supra* note 7, at 325-26 ("[S]trict tort . . . liability is often indistinguishable from liability for breach of the implied warranty of merchantability."); *id.* at 355:

of strict liability.⁷³ The existence of an "implied warranty" became the most common ground for decision.⁷⁴ The hybrid nature of the action for breach of warranty facilitated the adoption of this device.⁷⁵

It soon became clear that basing strict liability on a warranty notion created nearly as many problems as it seemed to solve. The term was so closely identified with contracts in the minds of most courts and lawyers that contract rules were assumed necessarily to apply.⁷⁶ This posed a problem if there was no contract.⁷⁷ Also, warranties on the sale of goods were governed by the Uniform Sales Act and later, in most states, by the Uniform Commercial Code. These statutes were intended primarily to govern the contractual relations between the seller and an immediate buyer.⁷⁸ Notice and disclaimer provisions⁷⁹ created formidable obstacles to recovery by a remote buyer. Such a buyer is unlikely to have any information about warranty or disclaimer terms.⁸⁰ Also, it may not occur to a remote buyer to give notice to a party with whom the buyer has had no dealings.⁸¹ These contractual defenses severely curtailed the usefulness of the strict liability doctrine.

A concluding question . . . is how the merchantability standard differs from the comparable strict tort standard The most obvious difference between the two standards is that the strict tort standard is considerably narrower in scope. It does not purport to reach all defective goods but only those that are not only defective but also "unreasonably dangerous," that is those that have the capacity to cause personal injury or property damage as opposed to those which cause only economic loss. Apart from that difference, we would find the terms nearly synonymous

73. Prosser, *The Assault*, *supra* note 66, at 1124.

74. *Id.* at 1125-26.

75. "A more notable example of legal miscegenation could hardly be cited than that which produced the modern action for breach of warranty. Originally sounding in tort, yet arising out of the warrantor's consent to be bound, it later ceased necessarily to be consensual, and at the same time came to lie mainly in contract."

Id. at 1126 (quoting Note, *Necessity for Privity of Contract in Warranties by Representation*, 42 HARV. L. REV. 414, 414-15 (1929)) (footnotes omitted).

76. Prosser, *The Assault*, *supra* note 66, at 1127.

77. W. PROSSER & W. KEETON, *supra* note 67, at 691.

78. *See* *Moorman Mfg. Co. v. National Tank Co.*, 91 Ill. 2d 69, 78, 435 N.E.2d 443, 447 (1982).

79. *See* notes 55-57 *supra* and accompanying text.

80. In a commercial setting, disclaimers allow the contracting parties to allocate the risks of a transaction as they wish. Disclaimers comport well with the general Code policy of allowing parties to make their own agreements. *See* U.C.C. § 2-715 comment 3 (1978) ("Any seller who does not wish to take the risk of consequential damages has available the section on contractual limitation of remedy [§ 2-719]."); U.C.C. § 2-719 comment 3 ("[Disclaimers] are merely an allocation of unknown or undeterminable risks."). However, if a manufacturer has disclaimed or limited warranties as to the first buyer, e.g., a wholesaler, the ultimate user or consumer may be bound by a warranty that he or she has neither seen nor bargained for. *See* U.C.C. § 2-318 comment 1.

81. U.C.C. § 2-607(3)(a) requires a party to give notice of a breach. As between immediate parties to a sale this is a sound rule, but as applied to remote parties who have been injured by defective products it becomes a "booby-trap for the unwary." *See* *Greenman v. Yuba Power Prods.*, 59 Cal. 2d 57, 377 P.2d 897, 27 Cal. Rptr. 697 (1963) (discussing the Uniform Sales Act, predecessor of the U.C.C.).

Courts resorted to a variety of devices to circumvent the notice and disclaimer provisions.⁸² This resort to "covert tools"⁸³ caused considerable consternation among legal commentators.⁸⁴ As the Reporter for the *Restatement (Second) of Torts*, Dean Prosser wrote and urged the adoption of section 402A, which extended strict tort liability from products "intended for intimate bodily use" to "any product."⁸⁵ Shortly before the new *Restatement* was adopted, the California Supreme Court decided *Greenman v. Yuba Power Products*,⁸⁶ recognizing, for the first time, a general tort theory of strict liability for defective products. Courts were quick to seize upon these developments as authority for discarding the warranty fiction and for recognizing a new theory of products liability sounding in tort.⁸⁷

82. Courts circumvented notice requirements by holding that a long delay before giving notice was "reasonable," e.g., *Whitfield v. Jessup*, 31 Cal. 2d 826, 193 P.2d 1 (1948), that the notice provisions did not apply to personal injuries, e.g., *Wright-Bachman, Inc. v. Hodnett*, 235 Ind. 307, 133 N.E.2d 713 (1956), or that the provision was inapplicable between parties who had not dealt with each other, e.g., *Ruderman v. Warner-Lambert Pharmaceutical Co.*, 23 Conn. Supp. 416, 184 A.2d 63 (C.P. 1962). See generally W. PROSSER & W. KEETON, *supra* note 67, at 691.

Courts often construed disclaimer provisions away, see, e.g., *Myers v. Land*, 314 Ky. 514, 235 S.W.2d 988 (1951), or held that the provisions were not brought home to the buyer, e.g., *Woodworth v. Rice Bros. Co.*, 110 Misc. 158, 179 N.Y.S. 722 (Sup. Ct. 1919), *affd.*, 193 A.D. 971, 184 N.Y.S. 958 (1920), *affd. per curiam*, 233 N.Y. 577, 135 N.E. 925 (1922), or simply held them invalid as contracts of adhesion or as contrary to public policy, e.g., *Henningsen v. Bloomfield Motors, Inc.*, 32 N.J. 358, 161 A.2d 69 (1960). See generally Prosser, *The Assault*, *supra* note 66, at 1132.

83. The phrase "covert tools" was coined by Karl Llewellyn. See Llewellyn, Book Review, 52 HARV. L. REV. 700, 703 (1939) ("The net effect is unnecessary confusion and unpredictability, together with inadequate remedy, and evil persisting that calls for remedy. Covert tools are never reliable tools.").

84. Karl Llewellyn remarked that:

[T]he actual need for remedy and reform is tremendous. . . . [T]he legal tools for giving any remedy are confused, are uncertain, don't guide trial courts and lead to a welter of appeals that is simply outrageous.

. . . .

If, for example, you proceed along the lines of warranty, then you run into court after court that says, "But a child can't have the remedy." You even run into a court that says, "When a wife buys, she buys as the assumed agent of her husband; therefore she has not got the remedy." You see, it is nuts, just nuts!

Wade, *supra* note 3, at 17-18 (quoting N.C.C.U.S.L., Minutes of the Committee of the Whole 88-93 (Sept. 1941) (unpublished typescript)).

Dean Prosser concluded that the use of warranty in these cases was "pernicious and unnecessary," because:

No one doubts that, unless there is privity, liability to the consumer must be in tort and not in contract. There is no need to borrow a concept from the contract law of sales; and it is "only by some violent pounding and twisting" that "warranty" can be made to serve the purpose at all. . . . If there is to be strict liability in tort, let there be strict liability in tort, declared outright, without an illusory contract mask.

Prosser, *The Assault*, *supra* note 66, at 1134.

85. See RESTATEMENT (SECOND) OF TORTS § 402A comment b (1965); 41 A.L.I. PROC. 349-75 (1964) (A.L.I. debate over proposed § 402A of the *Restatement (Second) of Torts*).

86. 59 Cal. 2d 57, 377 P.2d 897, 27 Cal. Rptr. 697 (1963) (holding manufacturer of defective power tool strictly liable in tort for personal injuries caused by the defect).

87. See, e.g., *Clary v. Fifth Ave. Chrysler Center*, 454 P.2d 244 (Alaska 1969); *Suvada v. White Motor Co.*, 32 Ill. 2d 612, 619-20, 210 N.E.2d 182, 186-87 (1965); *Goldberg v. Kollsman Instrument Corp.*, 12 N.Y.2d 432, 437, 191 N.E.2d 81, 83, 240 N.Y.S.2d 592, 595 (1963).

Unlike the Uniform Commercial Code, tort law generally regulates *forced* exchanges of entitlements.⁸⁸ Accidents are good examples. If an accidental injury occurs, and the injurer is adjudged liable, the injurer must pay (and the victim must accept) an objectively determined measure of damages.⁸⁹ Because subjective values are not taken into account, forced exchanges may not be *efficient*: both parties may end up worse off than before the accident.⁹⁰ In the paradigm case, it is impossible to rely on voluntary exchanges to reach an optimal result because the identities of the victim and the injurer are unknown until the accident occurs.⁹¹

In some cases the identities of potential injurers and potential victims *are* known. Depending on the circumstances, voluntary exchanges enforced by contract rules may lead to more efficient results. For example, while it seems inconceivable for drivers and pedestrians to bargain over the risk of traffic accidents, it may be feasible for coal miners and mine owners to bargain over wages that reflect the risk of mine accidents.⁹² The typical products liability situation presents another instance in which bargaining is feasible, because the potential injurer (the seller) and the potential victim (the buyer) are known.⁹³ When the buyer and the seller actually do bargain over the risk of injury due to a potentially defective product, the argument for applying contract rules is strongest.

Even if the buyer and seller expressly bargain over the risk of defects, the bargain may not be enforced because of overriding social policies.⁹⁴ The terms of a bargain may be set aside either because lim-

88. See generally Calabresi & Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972).

89. *Id.* at 1092.

90. See Calabresi & Melamed, *supra* note 88; Kronman, *Specific Performance*, 45 U. CHI. L. REV. 351, 351-63 (1978); Ulen, *The Efficiency of Specific Performance: Toward a Unified Theory of Contract Remedies*, 83 MICH. L. REV. 341, 375-376 (1984); cf. Note, *Beyond the Eye of the Beholder: Aesthetics and Objectivity*, 71 MICH. L. REV. 1438 (1973) (arguing that aesthetic values can be objectively measured).

91. A voluntary exchange would require that a bargain be struck between potential injurers and potential victims before the accident. Unless the potential injurers and potential victims already have a bargaining relationship, the transaction costs involved in this kind of pre-accident negotiation are likely to be prohibitive. G. CALABRESI, *THE COSTS OF ACCIDENTS* 90 (1970); Calabresi & Melamed, *supra* note 88, at 1108-09.

92. G. CALABRESI, *supra* note 91, at 90-91.

93. See Calabresi & Melamed, *supra* note 88, at 1109 n.38.

94. See *id.* The policy justifications for holding a seller strictly liable in tort are summarized in RESTATEMENT (SECOND) OF TORTS § 402A comment c (1965):

[T]he justification for the strict liability has been said to be that the seller, by marketing his product for use and consumption, has undertaken and assumed a special responsibility toward any member of the consuming public who may be injured by it; that the public has the right to and does expect, in the case of products which it needs and for which it is forced to rely upon the seller, that reputable sellers will stand behind their goods; that public policy demands that the burden of accidental injuries caused by products intended for consumption be placed upon those who market them, and be treated as a cost of production against which liability insurance can be obtained; and that the consumer of such products is entitled

iting the buyer to contract remedies would be unfair or because there was some defect in the bargaining process that prevented the parties from reaching an efficiency-enhancing result.

The fairness rationale is essentially comprised of the following four arguments. First, sellers convey to the public a general sense of product quality in their advertising and marketing practices, causing buyers to rely on them for their skill and expertise.⁹⁵ Second, sellers are often in a better position than buyers to identify potential product risks, to determine acceptable levels of such risks, and to confine the risks within those levels.⁹⁶ Third, most product accidents not caused by product abuse are probably attributable to the seller's negligence at some stage of the manufacturing or marketing process.⁹⁷ Fourth, sellers are almost invariably in a better position to absorb or spread the costs of product accidents.⁹⁸

The efficiency rationale typically is advanced by one of the following arguments. First, buyers are unable to protect themselves because of insufficient information, lack of bargaining power, or lack of choice.⁹⁹ Second, the costs of injuries flowing from defective products

to the maximum of protection at the hands of someone, and the proper persons to afford it are those who market the products.

See generally W. KEETON, D. OWEN & J. MONTGOMERY, *PRODUCTS LIABILITY AND SAFETY* 205-23 (1980); Owen, *Rethinking the Policies of Strict Products Liability*, 33 VAND. L. REV. 681, 703-14 (1980). One court described the development of strict tort liability as a response to the lack of contractual privity between manufacturer and ultimate user . . . ; the relatively unequal strengths of buyer and seller at the bargaining table . . . ; the difficulty faced by a consumer in proving negligence on the part of the manufacturer where the consumer is several steps down the distribution chain and the evidence of negligent production is exclusively within the control of the manufacturer . . . ; [and] the ability of the manufacturer to distribute the risk of loss among all its purchasers

General Pub. Utils. Corp. v. Babcock & Wilcox Co., 547 F. Supp. 842, 844 (S.D.N.Y. 1982) (citations omitted) (denying a tort cause of action against the seller of an allegedly defective nuclear reactor).

95. See RESTATEMENT (SECOND) OF TORTS § 402A comment c, *supra* note 94; see also W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 211; Owen, *supra* note 94, at 707-09.

96. See G. CALABRESI, *supra* note 91, at 90-91; W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 211; Owen, *supra* note 94, at 711-13.

97. See W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 212; Owen, *supra* note 94, at 710-11; see also Collins v. Eli Lilly Co., 116 Wis. 2d 166, 342 N.W.2d 37 (1984) (sale of defective and unreasonably dangerous product constitutes, assuming all the elements are proved, negligence per se); Wade, *Is Section 402A of the Second Restatement of Torts Preempted by the UCC and Therefore Unconstitutional?*, 42 TENN. L. REV. 123, 134-35 (1974) (negligence per se and *res ipsa loquitur* doctrines can be applied to reach the same results as strict tort liability).

98. See W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 212; Owen, *supra* note 94, at 710-11; see also RESTATEMENT (SECOND) OF TORTS § 402A comment c (1965) ("[P]ublic policy demands that the burden of accidental injuries caused by products . . . be treated as a cost of production against which liability insurance can be obtained . . .").

99. See Greenman v. Yuba Power Prods., 59 Cal. 2d 57, 63, 377 P.2d 897, 901, 27 Cal. Rptr. 697, 701 (1963) ("The purpose of [strict tort] liability is to insure that the costs of injuries resulting from defective products are borne by the manufacturers . . . rather than by the injured persons who are powerless to protect themselves."); G. CALABRESI, *supra* note 91, at 90-91; W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 211. But see A. SCHWARTZ & R. SCOTT, *COMMERCIAL TRANSACTIONS* 191 n.10 (1982) (bargaining power explanation fails to

can fairly be put on the enterprises marketing those products as a cost of doing business, thus assuring that these businesses will fully "pay their own way" in the society from which they derive their profits.¹⁰⁰ Finally, strict liability is needed to induce sellers to market safe products.¹⁰¹

The expansion of the judicially developed tort theory has brought it into conflict with the more restrictive warranty provisions of the Uniform Commercial Code. While some have argued that the area of products liability was preempted by legislative enactment of the Code, this view has not prevailed.¹⁰² Thus, in most states there are two potential remedies for the same wrong. In cases such as *Pennsylvania Glass Sand v. Caterpillar Tractor Co.*,¹⁰³ a commercial buyer in privity with its seller can escape the limitations on its warranty¹⁰⁴ by framing its cause of action in terms of strict tort liability. The following Part assesses whether allowing recourse to tort law under these circumstances can be justified in terms of the rationales for using strict liability to supplant the Code.

III. CHOOSING A RULE TO ACCOMMODATE THE POLICIES OF TORT LAW AND THE UNIFORM COMMERCIAL CODE

The tension between the policies of tort law and the Code develops because the function of the product is at the core of the parties' bargain.¹⁰⁵ Thus, the harm sustained by the defective product itself represents a loss of the buyer's bargain. This type of harm is specifically

account for the great similarity between written sales warranties in consumer and business markets).

100. See RESTATEMENT (SECOND) OF TORTS § 402A comment c (1965); W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 90, at 14.

101. W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 212; Owen, *supra* note 94, at 709-10.

102. *But see* note 4 *supra*; *see also* Wade, *supra* note 3, at 3 nn. 8 & 11. *See generally* Wade, *supra* note 97.

The preemption issue will take a somewhat different form if a federal products liability bill is passed. The provisions of that bill "[supersede] any state law regarding matters governed by [the] Act," thus apparently preempting both strict liability and liability for breach of warranty under the U.C.C. S. 44, 98th Cong., 1st Sess. § 3(a)-(c) (1983); *see also* Walters, *Federal Preemption of State Products Liability Laws and Limitations of the Strict Liability of Manufacturers*, 32 DRAKE L. REV. 961 (1983); Note, *The Products Liability Crisis: A Federal Statutory Solution*, 1983 ILL. L. REV. 757.

103. 496 F. Supp. 712 (M.D. Pa. 1980), *aff'd.*, 652 F.2d 1165 (3d Cir. 1981) (discussed at notes 18-21 *supra* and accompanying text).

104. *See* *Pennsylvania Glass Sand v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1176 (3d Cir. 1981); notes 55-59 *supra*. In *Pennsylvania Glass Sand*, the warranty limited the seller's liability to the replacement of defective parts and specifically excluded recovery for economic loss. 652 F.2d at 1167. The breach of warranty claim was also barred by the Code's statute of limitations, U.C.C. § 2-725 (1978), because the warranty did not explicitly extend to future performance. *See* 496 F. Supp. at 716; note 58 *supra* and accompanying text.

105. *See* *Miller Indus. v. Caterpillar Tractor Co.*, 733 F.2d 813, 817 (11th Cir. 1984) ("[T]he performance of the product — whether it explodes or fails to function — is conceptualized as part of the bargain . . ."); *Moorman Mfg. Co. v. National Tank Co.*, 91 Ill. 2d 69, 96, 435

addressed by the Uniform Commercial Code.¹⁰⁶ However, if buyers can characterize this harm as "property damage," they can avoid the warranty scheme of the Code — especially the warranty defenses available to the sellers¹⁰⁷ — by suing in tort.¹⁰⁸

There is some question as to whether strict liability remedies ought ever to be available to commercial buyers. Some courts have extended strict liability beyond consumer plaintiffs,¹⁰⁹ even though a commercial buyer is as likely to be able to absorb the loss or to spread it among its customers as the seller.¹¹⁰ Similarly, commercial buyers and sellers are likely to be equally aware of the risks they are undertaking and to bargain effectively for a contractual remedy.¹¹¹ Attempts by commercial buyers to exploit the property damage exception to the economic loss rule accentuate the anomaly of including commercial buyers in the strict tort liability scheme.¹¹²

N.E.2d 443, 455 (1982) (Simon, J., specially concurring) ("The product's function is at the core of the commercial bargain . . .").

106. See U.C.C. §§ 1-106(1), 2-714, 2-715 (1978); note 54 *supra* and accompanying text.

107. See notes 55-59 *supra* and accompanying text.

108. RESTATEMENT (SECOND) OF TORTS § 402A comment m (1965) states:

The rule stated in this Section is not governed by the provisions of the Uniform Sales Act, or those of the Uniform Commercial Code, as to warranties; and it is not affected by limitations on the scope and content of warranties, or by limitations to "buyer" and "seller" in those statutes. Nor is the consumer required to give notice to the seller of his injury within a reasonable time after it occurs, as is provided by the Uniform Act. The consumer's cause of action does not depend upon the validity of his contract with the person from whom he acquires the product, and it is not affected by any disclaimer or other agreement, whether it be between the seller and his immediate buyer, or attached to and accompanying the product into the consumer's hands.

109. See, e.g., *Keystone Aeronautics Corp. v. R.J. Enstrom Corp.*, 499 F.2d 146 (3d Cir. 1974); *Sterno Aero AB v. Page Airmotive, Inc.*, 499 F.2d 709 (10th Cir. 1974); *ICI Austl. Ltd. v. Elliott Overseas Co.*, 551 F. Supp. 265 (D.N.J. 1982). But see *Scandinavian Airlines Sys. v. United Aircraft Corp.*, 601 F.2d 425 (9th Cir. 1979), *Southwest Forest Indus. v. Westinghouse Elec. Corp.*, 422 F.2d 1013 (9th Cir.), *cert. denied*, 400 U.S. 902 (1970); *Avenell v. Westinghouse Elec. Corp.*, 41 Ohio App. 2d 150, 324 N.E.2d 583 (1974).

110. Some courts have grounded their adoption of strict liability on the manufacturer's superior ability (in relation to the consumer plaintiff) to spread the costs of accidents. See, e.g., *Santor v. A & M Karagheusian, Inc.*, 44 N.J. 52, 65, 207 A.2d 305, 312 (1965); see also *Seely v. White Motor Co.*, 63 Cal. 2d 9, 24, 403 P.2d 143, 155, 45 Cal. Rptr. 17, 27 (1965) (Peters, J., concurring and dissenting). When a commercial buyer is involved, however, it is not necessarily true that the seller is better able to spread the risks. See *Scandinavian Airlines Sys. v. United Aircraft Corp.*, 601 F.2d 425, 428 (9th Cir. 1979); *Kaiser Steel Corp. v. Westinghouse Elec. Corp.*, 55 Cal. App. 3d 737, 748, 127 Cal. Rptr. 838, 845 (1976); Note, *Disclaimers of Warranty in Consumer Sales*, 77 HARV. L. REV. 318, 327-28 (1963).

111. See *Sanco, Inc. v. Ford Motor Co.*, 579 F. Supp. 893, 897 (S.D. Ind. 1984), *affd.*, 771 F.2d 1081 (7th Cir. 1985); *General Pub. Utils. Corp. v. Babcock & Wilcox Co.*, 547 F. Supp. 842, 844 (S.D.N.Y. 1982).

112. This view of strict liability is not universally accepted:

The applicability of a tort theory depends not upon the size of the plaintiff, but upon the nature of the claim. The very attempt to distinguish tort rights on the basis of economic strength would raise collateral issues An actor has no more privilege to inflict injury on the wealthy than on the poor. The same rules apply to all, plaintiff or defendant, large or small. . . . [T]he doctrine of strict tort liability is not limited to "ordinary consumers."

Salt River Project Agric. Improvement & Power Dist. v. Westinghouse Elec. Corp., 143 Ariz. 368, 382, 694 P.2d 198, 212 (1984).

Even assuming, however, that strict liability remedies should sometimes be made available to commercial buyers,¹¹³ the contractual scheme set out in the Uniform Commercial Code is better suited for governing relations between commercial parties who are in privity. Allowing commercial buyers to sue their immediate sellers on a strict tort liability theory effectively overrides the parties' contractual allocation of risk. The tort remedy directly vitiates the effectiveness of section 2-316 of the Code, which allows warranties to be disclaimed,¹¹⁴ and section 2-725 of the Code, which establishes a four-year statute of limitations.¹¹⁵ More broadly, it impairs the general Code policies of uniformity and certainty in commercial transactions.¹¹⁶

Leaving commercial buyers to their remedies under the Code by no means assures harsh results, because the Code — which was developed before strict liability emerged — affords a buyer considerable protection.¹¹⁷ The Code creates implied warranties¹¹⁸ and requires basically that disclaimers be in writing, conspicuous, and consistent with express warranties.¹¹⁹ A court can refuse to enforce oppressive warranty terms against a buyer on unconscionability grounds.¹²⁰ A court

113. Affording a commercial buyer a cause of action based on strict tort liability against a remote manufacturer may be justifiable if the manufacturer's disclaimer or limitation on warranties is held to be effective against an ultimate purchaser who did not have the opportunity to negotiate over the terms of the agreement. See U.C.C. §§ 2-316, 2-719 (1978). This is still an unresolved issue. See J. WHITE & R. SUMMERS, *supra* note 7, at 409; see also *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 98 N.J. 555, 582, 489 A.2d 660, 674 (1985) (reserving determination on the operation of U.C.C. remedies against remote parties, but holding strict liability action inapplicable against remote manufacturer).

114. See notes 55-56 *supra* and accompanying text.

115. See notes 58-59 *supra* and accompanying text.

116. See note 46 *supra* and accompanying text. For example, consider *James v. Bell Helicopter Co.*, 715 F.2d 166 (5th Cir. 1983), an action brought by a Utah buyer against a Texas seller and an Illinois clutch manufacturer. Applying Texas law, the court affirmed dismissal of the tort claim against the seller. Applying Illinois law, the court reversed dismissal of the tort claim against the clutch manufacturer. See also Wade, *supra* note 3, at 27:

The law in one state may adversely affect all three parties to a personal injury case — manufacturer, insurer, and injured party — in other states. The manufacturer's products may be distributed in many states, even nationwide. He must give due consideration to the liability law of all the states where he distributes, and this may affect the nature and cost of his products. The insurance companies are not accustomed to calculating insurance rates according to the actuarial experiences in the individual states. If a state in the northeast or on the west coast develops a rule that is unusually favorable to the injured party, insurance rates and product costs may both rise in other states without any corresponding benefit to the consumer. One of the ironies of the legislative splurge to put restrictions and limitations on liability actions to relieve the products liability crisis was that such an act in a particular case lessened the protection for the local consumer without affording any actual relief to the local manufacturer.

117. See notes 119-22 *infra*; see also Wade, *supra* note 97, at 132-36 (contending that a provision similar to § 402A had been dropped from the U.C.C. in favor of § 2-318, which extends sales warranties to certain third parties).

118. See notes 52-53 *supra* and accompanying text.

119. See U.C.C. § 2-316 (1978). The federal Magnuson-Moss Warranty Act, 15 U.S.C. §§ 2301-2312 (1982), also applies in the case of consumer goods. See J. WHITE & R. SUMMERS, *supra* note 7, at 367-74.

120. U.C.C. § 2-302 (1978); see also *Sanco, Inc. v. Ford Motor Co.*, 579 F. Supp. 893, 897

can also grant relief if it finds that circumstances cause an exclusive remedy to "fail of its essential purpose."¹²¹ In addition, the Code imposes a general obligation to deal in good faith.¹²² Finally, the Code defenses, such as a failure to give notice of breach, are considerably less onerous for a buyer who has had previous dealings with the seller.¹²³

At the same time, the policies that justify strict liability have considerably less force when a commercial buyer is suing an immediate seller for the value of the product. When the buyer and seller are in privity, there is no difficulty in identifying the potential victims and the potential injurer. This significantly reduces the transaction costs of allocating the risk of defects by contract.¹²⁴ Of course, sellers will sometimes be in a better position than buyers to minimize the risks of product defects. However, informed buyers will at other times have a comparative advantage over sellers in minimizing the risks posed by those defects.¹²⁵ The parties and society as a whole will be better off if

(S.D. Ind. 1984) ("The fact that courts are reluctant to invoke these [unconscionability] provisions does not justify the application of tort theory to resolve a problem of sales law."), *aff'd*, 771 F.2d 1081 (7th Cir. 1985); *Clark v. International Harvester Co.*, 99 Idaho 326, 335, 581 P.2d 784, 793 (1978) ("[T]he UCC provisions provide this Court with ample room for the exercise of wide judicial discretion to ensure that substantial justice results in particular cases."); *Monsanto Co. v. Alden Leeds, Inc.*, 130 N.J. Super. 245, 262, 326 A.2d 90, 99 (Super. Ct. Law Div. 1974) ("[A] hearing must be held as to the contract's commercial setting, purpose and effect, in order to aid the court in determining whether the clause is unconscionable under the circumstances."); *Lobianco v. Property Protection Inc.*, 292 Pa. Super. 346, 369, 437 A.2d 417, 429 (1983) (Montgomery, J., dissenting) ("[U.C.C. § 2-302] appears to permit the exercise of broad discretion by a court in determination of whether a clause may be unconscionable in the circumstances of any particular case."); U.C.C. § 2-719(3) (making certain warranty limitations unconscionable). *But see* *Moorman Mfg. Co. v. National Tank Co.*, 92 Ill. App. 3d 136, 145, 414 N.E.2d 1302, 1310 (1980) (the reluctance of courts to invoke good faith and unconscionability clauses and the development of strict tort liability is testimony to the inadequacies of the U.C.C.), *rev'd. in part*, 91 Ill. 2d 69, 435 N.E.2d 443 (1982); J. WHITE & R. SUMMERS, *supra* note 7, at 475-76 (U.C.C. § 2-316 may preempt the unconscionable doctrine in commercial disclaimer cases).

121. U.C.C. § 2-719(2) (1978); *see, e.g.*, *Rudd Constr. Equip. Co. v. Clark Equip. Co.*, 735 F.2d 974, 982 (6th Cir. 1984) (limited remedy of equipment repair fails of essential purpose where equipment totally destroyed). Ironically, the paradigm "failure of essential purpose" case is one in which a product is damaged beyond repair as the result of its own defects and its warranty is limited to repair or replacement of defective parts. *See* J. WHITE & R. SUMMERS, *supra* note 7, at 465-71. Thus recourse to a strict tort liability claim in this context is critical only to a buyer who must circumvent the Code's statute of limitations, U.C.C. § 2-725 (1978), to recover.

122. U.C.C. § 1-203 (1978); *see* *Sanco, Inc. v. Ford Motor Co.*, 579 F. Supp. 893, 897 (S.D. Ind. 1984) (dicta) (reluctance of courts to invoke "good faith" provision does not justify application of tort theory to resolve a sales law problem).

123. *See* note 81 *supra*.

124. *See* notes 88-93 *supra* and accompanying text.

125. *See* A. SCHWARTZ & R. SCOTT, *supra* note 99, at 190; *see also* Calabresi, *Optimal Deterrence and Accidents*, 84 YALE L.J. 656, 657 (1975) (if there is no liability without negligence, optimal deterrence will be achieved only if the victim class *always* can (1) best decide whether accident avoidance is worthwhile; and (2) best accomplish such worthwhile avoidance); Calabresi & Hirschhoff, *Toward a Test for Strict Liability*, 81 YALE L.J. 1055, 1060-61 (1972) (liability should be imposed on the party relatively more likely to find out whether accident avoidance is worth it — the cheapest cost avoider).

the buyer and seller are allowed to allocate risks consistent with their respective advantages.¹²⁶ These potential gains are forgone if a risk allocation is imposed by law.

Thus, the fairness and efficiency rationales for strict liability are not compelling in the commercial context. Because social wealth may increase if the parties are permitted to allocate the risks of product defects by contract, the efficiency rationale¹²⁷ is substantially weakened. Because the buyer is protected to a considerable extent by the Code, the fairness rationale¹²⁸ is also weakened. Nevertheless, several justifications have been advanced for permitting a commercial buyer to recover for a product's self-inflicted damage in spite of limitations on the seller's liability contained in an express warranty or in the Code.

One common justification for allowing commercial buyers to recover the value of defective products in tort is the need to deter manufacturers from producing unreasonably dangerous products. If manufacturers are held strictly liable for defective products, the argument goes, they will produce safer products. Safe products, the argument continues, should not be something the parties are forced to bargain over; unreasonably dangerous products should simply not be produced.¹²⁹ Strict tort liability is thus extended to commercial buyers on the social policy grounds of improving safety generally.¹³⁰

This justification suffers from a logical difficulty in the strict tort liability context. Once we know a product is "bad," i.e., unreasonably dangerous, it makes sense to deter its manufacturer from producing it.¹³¹ But the deterrence argument contributes nothing to deciding what type and degree of residual danger makes a product "bad" in the first place. It offers no basis for distinguishing an unreasonably dangerous product from one that entails reasonable risks.¹³²

This failure of the deterrence justification to distinguish unreasonably dangerous products from those that entail an acceptable level of risk is especially problematic in the commercial context. Imposing strict liability based on a deterrence rationale will tend to discourage

126. See note 61 *supra*; note 141 *infra*.

127. See notes 99-101 *supra* and accompanying text.

128. See notes 95-98 *supra* and accompanying text; see also *Jig the Third Corp. v. Puritan Marine Ins. Underwriters Corp.*, 519 F.2d 171, 180 (Gee, J., dissenting) ("[A]llowing the plaintiff . . . to prosecute its tort cause of action is highly unfair to the defendant . . . [where the parties are in a contractual relationship].").

129. See, e.g., *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1175 (3d Cir. 1981); *Salt River Project Agric. Improvement & Power Dist. v. Westinghouse Elec. Corp.*, 143 Ariz. 368, 381, 694 P.2d 198, 211 (1984).

130. See Note, *Contract or Tort*, *supra* note 3 at 509-10.

131. But see Henderson, *Product Liability and the Passage of Time: The Imprisonment of Corporate Rationality*, 58 N.Y.U. L. REV. 765 (1983) (real-world phenomena inhibit the effect of court-created incentives to produce safer products).

132. Owen, *supra* note 94, at 709-10.

the sale of all products that pose any significant danger.¹³³ When commercial parties with comparable bargaining power and access to information negotiate a warranty concerning a potentially dangerous product, they presumably have made their own judgment about the risks and potential benefits associated with the product, with the buyer concluding that the expected benefits outweigh the expected costs.¹³⁴ It is precisely this type of bargain that the Uniform Commercial Code is designed to protect.¹³⁵ Strict tort liability effectively overrides the parties' judgment and undermines Code policies.

Further, it is economically inefficient to negate the terms of the parties' bargain unless there is some reason (excluding hindsight) to believe that a court is better equipped to weigh product risks and benefits.¹³⁶ A general refusal to enforce contract terms leads to more efficient results only if buyers systematically and persistently underestimate product risks.¹³⁷ In the commercial context, any errors by the buyer in estimating product risks are likely to be random, and buyers are likely to know the terms of their contracts and the range of market alternatives. Thus, the imposition of strict tort liability in the commercial setting is likely to lead to a less than optimal allocation of risk.

Another common justification for strict tort liability is that manufacturers should *always* bear the cost of accidents caused by their defective products, either because manufacturers are better able to minimize product defects or better able to spread the cost of injuries among their buyers.¹³⁸ In cases involving commercial entities, however, the assumptions on which this rationale is founded may be fundamentally incorrect. As a matter of economic efficiency, allocating

133. See Owen, *supra* note 94, at 709; Sachs, *Negligence or Strict Products Liability: Is There Really a Difference in Law or Economics?*, 8 GA. J. INTL. & COMP. L. 259, 274-76 (1978); see also INTERAGENCY TASK FORCE ON PRODUCTS LIABILITY, U.S. DEPT. OF COMMERCE, FINAL REPORT, *supra* note 30, at VI-47; W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 54-55; Cowan, *Some Policy Bases of Products Liability*, 17 STAN. L. REV. 1077, 1087-92 (1965); Shavell, *Strict Liability Versus Negligence*, 9 J. LEGAL STUD. 1 (1980); Weinstein, Twerski, Piehler & Donaher, *Product Liability: An Interaction of Law and Technology*, 12 DUQ. L. REV. 425, 430-33 (1974).

134. Cf. note 141 *infra*.

135. See notes 63-64 *supra* and accompanying text.

136. See Schwartz & Wilde, *Imperfect Information in Markets for Contract Terms: The Examples of Warranties and Security Interests*, 69 VA. L. REV. 1387, 1457-58 (1983). A general ban on the enforcement of warranty terms is only appropriate for transactions involving frequently purchased, inexpensive items, which malfunction so as to cause personal injury a very low percentage of the time. Strict tort liability is one means of implementing such a general ban. *Id.* at 1458-59 & nn.120-21. The standard example is the exploding soda bottle. Cf. *Escola v. Coca Cola Bottling Co.*, 24 Cal. 2d 453, 150 P.2d 436 (1944).

137. See Schwartz & Wilde, *supra* note 136, at 1458-59. Although the authors focus on consumer warranties, their analysis can be applied to the commercial setting as well. See *id.* at 1416 & n.53.

138. See, e.g., *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1172-73 (3d Cir. 1981); see also notes 96 & 98 *supra* and accompanying text.

the risk of all product defects to sellers by law may prevent the parties from taking advantage of the buyer's superior ability to avoid certain risks.¹³⁹ It seems likely that there will be at least some product risks that the buyer, rather than the seller, will be able to avoid more cheaply or insure against more readily.¹⁴⁰ Moreover, substituting a legal allocation of risks for one that may have been bargained for by the parties¹⁴¹ is at odds with the Code's policy of allowing parties to negotiate their own contracts.¹⁴² Indeed, strict liability creates substantial information demands on the legal system by requiring courts to formulate their own complex risk allocation judgments.¹⁴³

When a product is damaged as a result of its own defects, commercial buyers¹⁴⁴ in privity with the defendant should be left to the reme-

139. See A. SCHWARTZ & R. SCOTT, *supra* note 99, at 191-96; Calabresi, *supra* note 125, at 657; Calabresi & Hirschhoff, *supra* note 125, at 1058; Coase, *The Problem of Social Cost*, 35 J. LAW & ECON. 1, 3 (1960); Posner, *Strict Liability: A Comment*, 2 J. LEGAL STUD. 205, 209 (1973).

140. See A. SCHWARTZ & R. SCOTT, *supra* note 99, at 191-96; Calabresi, *supra* note 125, at 657; Calabresi & Hirschhoff, *supra* note 125, at 1058.

141. See note 61 *supra*; Posner, *supra* note 139, at 208.

Regardless of liability, the seller will have an incentive to adopt any cost-justified precaution, because, by lowering the total cost of the product to the buyer, it will enable the seller to increase his profit. Where, however, the buyer can prevent the accident at lower cost than the seller, the buyer can be counted on to take the precaution rather than the seller, for by doing so the buyer will minimize the sum of the price of the product (which will include the cost of any precautions taken by the seller) and the expected accident cost.

(footnotes omitted). Posner uses the following example:

Suppose the price of a product is \$10 and the expected accident cost 10¢; then the total cost to the (risk-neutral) consumer is \$10.10. If the producer can reduce the expected accident cost to 5¢ — say at a cost of 3¢ to himself — then he can increase the price of the product to \$10.05, since the cost to the (risk-neutral) consumer remains the same. Thus his profit per unit is increased by 2¢.

Id., at 208 n.7.

142. See notes 56-60 *supra* and accompanying text.

143. The problem is that it takes a lot of information to decide what degree of risk is "unreasonable." See generally W. KEETON, D. OWEN & J. MONTGOMERY, *supra* note 94, at 491-506; see also Calabresi & Hirschhoff, *supra* note 125, at 1060; Epstein, *A Theory of Strict Liability*, 2 J. LEGAL STUD. 151, 169-70 (1973); Posner, *supra* note 139, at 211-12.

144. Limiting the privity approach to commercial buyers is necessary in light of the economic rationales put forward for that approach. However, the underlying distinction between commercial buyers and consumers is problematic. Although some courts have relied heavily upon the plaintiff's character as a commercial buyer, see, e.g., *Twin Disc, Inc. v. Big Bud Tractors*, 582 F. Supp. 208 (E.D. Wis. 1984); *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 98 N.J. 555, 574-77, 489 A.2d 660, 670-71 (1985), small commercial buyers occasionally find themselves in need of the same protections afforded to consumers. Courts employing the commercial/consumer distinction have shown a willingness to manipulate the definition of "consumer" to encompass these cases. E.g., *Sterno Aero AB v. Page Airmotive, Inc.*, 499 F.2d 709 (10th Cir. 1974); *Moorman Mfg. Co. v. National Tank Co.*, 92 Ill. App. 3d 136, 144, 414 N.E.2d 1302, 1309 (1980), *rev'd in part*, 91 Ill. 2d 69, 435 N.E.2d 443 (1982); *Spring Motors Distribs., Inc. v. Ford Motor Co.*, 191 N.J. Super. 22, 40-41, 465 A.2d 530, 541 (Super. Ct. App. Div. 1983), *rev'd*, 98 N.J. 555, 489 A.2d 660 (1985); see also *ICI Austl. Ltd. v. Elliott Overseas Co.*, 551 F. Supp. 265 (D.N.J. 1982) (commercial purchaser may recover in strict liability action). The analysis of Judge Peters in *Seely v. White Motor Co.*, 63 Cal. 2d 9, 27-28, 403 P.2d 145, 157-58, 45 Cal. Rptr. 17, 29-30 (1963) (Peters, J., concurring in judgment), is typical of these cases:

Although this is a close case, I would find that plaintiff was an ordinary consumer insofar as the purchase involved here was concerned, even though he bought the truck for use in

dies provided by the Uniform Commercial Code. Strict tort liability should apply only when the buyer and seller are not in privity. The privity limitation makes sense when only the defective product itself is damaged, because in these situations the affected parties have allocated the risk of product defects by contract. Such bargaining between rational decisionmakers will tend to produce efficient results.¹⁴⁵ When there is some reason to suspect that the bargaining process has been unfair or has led to inefficient results, Code provisions are available to grant relief on a case-by-case basis.¹⁴⁶

The privity limitation is consistent with the policies underlying strict liability when a product is damaged because it does not preclude a tort recovery by third parties who would otherwise be forced to bear the external costs of the transaction. The privity limitation is consistent with Code policy in this context because it promotes certainty and stability in commercial transactions. Finally, the privity limitation is a common law doctrine that can be applied far more easily than can rules requiring judicial appraisal of the nature of the defect, the type of risk, and the manner in which the injury arose.¹⁴⁷

CONCLUSION

When a commercial buyer is in privity with its seller, recovery for the value of a defective product should be controlled by the Uniform Commercial Code. If the damage is to the product itself and the parties have allocated the risk of defects contractually, allowing a strict liability action unfairly allows commercial buyers to escape the consequences of their bargain.¹⁴⁸ Even in the absence of bargaining over risks, strict liability is economically inefficient because it introduces an element of uncertainty into commercial transactions, thereby increasing transaction costs and creating incentives to overinvest in safety. Strict liability frustrates Code policies by interfering with the ability of parties to allocate resources between them as they see fit. Finally, it is

his business. Plaintiff was an owner-driver of a single truck he used for hauling and not a fleet-owner who bought trucks regularly in the course of his business. He was the final link in the marketing chain, having no more bargaining power than does the usual individual who purchases a motor vehicle on the retail level.

I recognize that this "ordinary consumer" test needs judicial definition. This should be done on a case-by-case basis as is customarily done with any new doctrine. It is, however, the best resolution of the dilemma facing this court.

Although the distinction is currently unstable, the "commercial buyer" limitation should normally have little effect on results, for ordinary consumers are unlikely to be in privity with manufacturers.

145. See notes 60-61 *supra* and accompanying text.

146. See Schwartz & Wilde, *supra* note 136, at 1458-59; notes 120-22 *supra* and accompanying text.

147. See notes 25-39 *supra* and accompanying text.

148. See, e.g., *Rudd Constr. Equip. Co. v. Clark Equip. Co.*, 735 F.2d 974, 984 (6th Cir. 1984) ("[W]e do not believe that a sophisticated, commercial buyer like Rudd can evade contractual language excluding liability . . . simply by suing the seller in tort.").

unnecessary because commercial buyers can protect themselves contractually.¹⁴⁹

— Mark A. Kaprelian

149. Probably the most common situation in which a commercial buyer sues a seller on a strict tort liability theory is where the Code's four-year statute of limitations, U.C.C. § 2-725 (1978), has expired. *See, e.g.,* Pennsylvania Glass Sand v. Caterpillar Tractor Co., 652 F.2d 1165 (3d Cir. 1981); Cinnaminson Twp. Bd. of Educ. v. U.S. Gypsum Co., 552 F. Supp. 855 (D.N.J. 1982); ICI Austl. Ltd. v. Elliot Overseas Co., 551 F. Supp. 265 (D.N.J. 1982); Largoza v. General Elec. Co., 538 F. Supp. 1164 (E.D. Pa. 1982); Vulcan Materials Co. v. Driltech, Inc., 251 Ga. 383, 306 S.E.2d 253 (1983); Moorman Mfg. Co. v. National Tank Co., 91 Ill. 2d 69, 435 N.E.2d 443 (1982); Spring Motors Distribs., Inc. v. Ford Motor Co., 191 N.J. Super. 22, 465 A.2d 530 (Super. Ct. App. Div. 1983), *revd.*, 98 N.J. 555, 489 A.2d 660 (1985). This problem can be avoided by negotiating a warranty that "explicitly extends to future performance." U.C.C. § 2-725(2) (1978); *see* note 58 *supra* and accompanying text.

A commercial buyer could also assert that the circumstances caused an exclusive or limited remedy to "fail of its essential purpose." U.C.C. § 2-719(2) (1978); *see* J. WHITE & R. SUMMERS, *supra* note 7, at 465-71; note 121 *supra* and accompanying text. A commercial buyer could also conceivably allege unconscionability if it has agreed to a limited warranty. *See* note 120 *supra* and accompanying text.